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Subject: Paulson's returns falter again; investors fret

RPT-INSIGHT-John Paulson's
returns falter again; investors fret

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By Svea Herbst-Bayliss
(Reuters) - Billionaire trader John Paulson has told his wealthy investors that he has learned from his mistakes of 2011, which produced enormous losses for his closely watched hedge fund.
The founder and manager of Paulson & Co, who made his fortune and fame by betting against the subprime mortgage market, went so far as to tell investors in January that last year's big losses, including a 50 percent decline in his popular Advantage Plus fund, were an "aberration."
But as the months tick on, many investors are still waiting to see the dramatic turnaround Paulson has vowed to deliver.
Halfway through 2012, Advantage Plus is down again, losing 10 percent through May. Another big portfolio that bets on gold - once a bright spot for Paulson - was also in the red. In both cases, he blamed losses in gold stocks for the declines.
This has taken a huge bite out of the firm's assets, which have fallen to $22 billion from $38 billion early last year, according to investors. Redemptions were substantial, but poor performance accounted for the bulk of the drop, they said.
While Paulson still has loyal clients, some U.S. public pension funds and Wall Street firms that are invested with him have expressed their growing unease.
There are few signs of a quick comeback for the 56-year-old trader, who fumbled in 2012 by missing out on a big first-quarter rally in U.S. financial stocks. Last year, a Paulson fund got pounded by being too bullish on banks. He cut some of those losing positions - most notably by exiting Bank of America Corp in late 2011, just before the rebound.
Adding more pressure are some rare defections as two of his top lieutenants - Robert Lacoursiere, a former partner, and banking analyst James Fotheringham - left in March to start their own fund, Petrarca Capital.
"It is fair to say that he is having a difficult year," said Steve Yoakum, executive director of the $30 billion Missouri Public Employee Retirement System, which is invested with him.
New Mexico, which stuck by Paulson through last year's growing losses, pulled its $40 million investment in the first quarter.
"From time to time, I do check on John Paulson to see whether we did the right thing," said Joelle Mevi, the state's chief investment officer. "And I see that we did."
Mevi, who oversees $11.9 billion in public pension money, said New Mexico had decided to cash out in part because of concerns that the manager's fund had become too large and could not easily get in and out of positions.
At least one Wall Street bank that raked in big fees selling access to Paulson's funds over the years is souring on him. The brokerage arm of Morgan Stanley put Paulson on a "watch list" early in the second quarter, instructing clients to avoid putting new money with him.
To be sure, Merrill Lynch, UBS AG and other banks whose brokerage arms also offer access to Paulson funds have not taken similar steps.
And some of Paulson's other portfolios were doing better and posted gains in the first five months of 2012.
Charles Krusen, chief executive officer of Krusen Capital Management, says he thinks Paulson has

taken key steps to reposition the portfolio by hedging better and pulling back some of his positions.
"Going into the second half of 2012, he is well-positioned," Krusen said.
A spokesman for Paulson declined to comment for this story.

MISTAKES WERE MADE

Paulson has admitted to his investors that in 2011 he was overly optimistic about the speed of the U.S. recovery and underestimated the magnitude of Europe's debt crisis. He has called last year's performance "unacceptable" and said he was committed to delivering a "superior investment performance" in the future.
Some analysts who study the $2 trillion hedge fund industry say Paulson may have miscalculated again this year.
Known for his patient, or some might say stubborn, views, Paulson is sticking with gold stocks, saying they are undervalued compared with the price of the metal.
He told investors these stocks had helped performance from late May through early June, but for the year to date, two of his big holdings have not performed well. AngloGold Ashanti is down nearly 20 percent on the New York Stock Exchange, while Gold Fields Ltd's ADRs have fallen nearly 17 percent.
Another criticism is that Paulson is late trying to capitalize on bets that the crisis in the euro zone will mean hard times for the continent's banks and financial institutions.
Paulson has told investors that his team has spent a lot of time thinking about Europe and possible calamities that could occur there, including a Greek payment default.
If Greece does default and exits the common currency, he said, European banks would be hit extremely hard.
"He seems anxious to be shorting Europe, but he needs an event to succeed, such as a bank failure, but the European Central Bank and European Union officials have so far obviated that," said Peter Rup, CEO and chief investment officer at Artemis Wealth Advisors, which is not invested with Paulson.
As they tweak the portfolio, Paulson and his team are spending a lot of time trying to persuade jittery investors to stick with him and newcomers to put money with him.
One New York adviser to wealthy clients recently expressed surprise at how much time Paulson, one of the industry's busiest managers, had spent explaining his views on the world and investing to him. The adviser requested anonymity because his employer forbids him to speak to the media.
Paulson, who mostly avoids the society pages and big-name events that some of his rivals seek out, has also been attending more industry gatherings.
In May, for the first time, he presented his "best ideas" at the Ira Sohn Investment Conference, a popular charity event attended by a number of well-known managers. But the idea Paulson presented was anything but new: He listed AngloGold Ashanti, a long-term holding, as one of his favorite picks.
He previously let his 2007 returns speak for him. That year, largely on the strength of the subprime trade, his credit fund surged 591 percent, and the Advantage Plus fund rose 163 percent.

UNDER PRESSURE

There are signs that the pressure to deliver may be getting to the normally soft-spoken manager, who has long said that he and his partners put up more than half of his firm's capital.
Earlier this year, he shouted impatiently on a conference call, urging management at Hartford Financial Services Group Inc , another big holding, to consider splitting up the company.
Investors have only a few chances to pull their money out of his various funds every year. To do so by the end of June, they would have had to notify Paulson by mid-May, according to several smaller investors who said they had asked for their money back.
Investors have said Paulson has signaled that second-quarter redemptions will add up to the usual few percent of past quarters.
But if the numbers do not show improvement soon, industry analysts worry that confidence may weaken further, especially if other big clients like state pension funds begin to bolt.
"We don't have a formal watch list, but he is being watched more closely," Missouri's Yoakum said. "And we are certainly much more critical than we have been in the past."